

STATE OF MICHIGAN
IN THE SUPREME COURT

On appeal from the Court of Appeals, Gleicher, P.J., and Sawyer and Fort Hood, JJ.

DANNY EPPS and JOYCE EPPS,

Plaintiffs-Appellees/Cross-
Appellants,

v

4 QUARTERS RESTORATION, L.L.C.,
DENAGLEN CORP., d/b/a MBM CHECK
CASHING, EMERGENCY INSURANCE
SERVICES, and TROY WILLIS,

Defendants-Appellants/Cross-
Appellees.

Supreme Court No. 147727

Court of Appeals No. 305731

Wayne County Circuit Court
LC No. 09-018323-NO

147727
reph

DEFENDANTS-APPELLANTS' REPLY BRIEF IN
SUPPORT OF APPLICATION FOR LEAVE TO APPEAL

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FILED

NOV 15 2013

LARRY S. ROYSTER
CLERK
MICHIGAN SUPREME COURT

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ARGUMENT

I. Substantial Grounds Exist for Granting Defendants' Application for Leave.

In their answer to Defendants' application for leave to appeal, Plaintiffs contend that no grounds exist for granting Defendants' application. In truth, solid grounds exist under MCR 7.302(B)(3) and (B)(5) for granting Defendants' application.

The issues raised by Defendants in the application for leave to appeal involve legal principles of major significance to the state's jurisprudence in several regards.

MCR 7.302(B)(3). It is very important that this Court reverse some alarming rulings in the Court of Appeals opinion that will have a very negative effect on the state's jurisprudence if those rulings are perpetuated. First, the Court of Appeals has held (1) that fraudulent representations inducing the execution of a contract render the contract documents void *ab initio* and (2) that transfers of property to an innocent third party for value pursuant to powers granted in the contract documents can be upset and large losses imposed on the innocent third parties who have received the transfers in their business. The general rule existing heretofore has been (1) that fraudulent misrepresentations inducing the execution of a contract makes the contract only voidable and not void and (2) that transfers of property for value made to an innocent a third party, such as Defendant Denaglen d/b/a MBM Check Cashing, pursuant to a voidable contract are effective and cannot be unwound to the detriment of the innocent third-party transferee. Under the ruling here, the innocent third party (Defendant Denaglen) stands to lose \$128,000 by virtue of the ruling that the contract documents upon which Denaglen relied (in taking a transfer of checks from Defendant Troy Willis for value) should be treated as void *ab initio* based on alleged misrepresentations made by Willis in inducing Plaintiffs to sign the contracts. It is extremely important to state's jurisprudence, and to the business climate of the State of Michigan, that illogical results—such as the treatment of the contract documents as void *ab initio*

and imposing a large loss on the innocent transferee—be corrected and eliminated.

It is also of major significance to the state's jurisprudence that this Court apply MCL 440.3420(2) for the first time in a reported decision and make it clear that a plaintiff in a case involving conversion of negotiable instruments, such as checks, cannot recover the face amount of the converted checks if the proceeds of the checks ended up going to the purpose for which the checks were intended or ended up being applied in a way that conferred benefit upon the payee of the check. Under MCL 440.3420(2), added to the Michigan UCC effective September 30, 1993, the amount of the recovery for a payee of a converted check may not exceed the amount of the payee's interest in the check. In this case, the checks cashed by Defendant Willis pursuant to the authority granted to him in an insurance power of attorney, and pursuant to an assignment of the check proceeds to his companies, were issued in the names of Plaintiffs for the purpose of having the check proceeds turned over to the Willis Defendants to pay for their restoration of the Plaintiffs' flooded basement and damaged personal property. Thus, Plaintiffs had no interest in the checks since the proceeds were assigned to the Willis Defendants and the monies were supposed to go the Willis Defendants to pay for the restoration work. The Court of Appeals erred in holding that Plaintiffs were entitled to recover the face amount of all of the insurance checks cashed by Defendant Willis because that ruling will result in a windfall for Plaintiffs since they will have the benefit of the restoration work and the recovery of the monies that were supposed to go to the Willis Defendants to pay for the work.

Furthermore, leave to appeal should be granted in this matter because the decision of the Court of Appeals is clearly erroneous and will cause material injustice. In addition, the decision of the Court of Appeals in this case conflicts with Michigan Supreme Court decisions and other decisions of the Court of Appeals. The decision in this case is clearly erroneous in holding that

the minor misrepresentations of the Willis Defendants (inducing Plaintiffs to sign contract documents for the restoration of their home) rendered the contract documents void *ab initio* and took away rights granted in those documents for the Willis Defendants to indorse the insurance checks and to receive check proceeds that were assigned to the Willis Defendants in the documents. The cases of *Whitcraft v Wolfe*, 148 Mich App 40, 52; 384 NW2d 400 (1985), and *Dunn v Goebel Brewing Co*, 357 Mich 693, 697; 99 NW2d 380 (1959), both hold that fraud inducing a party to execute a contract only renders the contract voidable and not void. In this case, it was clearly erroneous for the Court of Appeals to diverge from those precedents and to hold instead that the fraud in the inducement rendered the contract documents void *ab initio*. That ruling will cause material injustice because it improperly and retroactively takes away the authority upon which the Defendants relied in carrying out the cashing of the insurance checks.

The Court of Appeals decision was also clearly erroneous in holding that there was no factual issue as to the amount of damages under the UCC and that Plaintiffs were entitled to damages from Defendants in the amount of the face amount of the checks. Under MCL 440.3420(2), Plaintiffs were only entitled to recover an amount equal to their interest in the checks. Plaintiffs had little or no interest in the checks since all of the monies from the checks were applied to Plaintiffs' obligation to pay the Willis Defendants for the restoration work. Plaintiffs had no damages because they realized the full benefit of the checks by having in the check proceeds applied on their obligation to the Willis Defendants for the restoration work. Material injustice will result from the Court of Appeals decision because a windfall is being conferred upon Plaintiffs at the expense of Defendants, and particularly upon Defendant Denaglen (whose funds in the amount of \$128,000 are sitting in the interpleader fund created when Comerica Bank required Denaglen to consent to putting the funds from Denaglen's bank

account into the interpleader fund with the court.)

The Court of Appeals also clearly erred in failing to reverse the decision of the trial judge denying Denaglen's motion to set aside the default entered against Denaglen by Plaintiffs' attorney. That clearly erroneous decision is causing material injustice to Denaglen because Denaglen has been prevented from participating fully in the case and has been relegated to the sidelines having to argue that it is still entitled to a jury trial on the issue of damages and that the complaint of Plaintiffs failed to plead a viable claim for conversion of the insurance checks.

In addition, the decision of the Court of Appeals is clearly erroneous in essentially awarding to Plaintiffs the remedy of restitution of moneys realized from the insurance checks in a situation where Plaintiffs are not in a position to restore to the Willis Defendants the things of value provided by the Willis Defendants and have made no attempt to do equity for Defendants. The remedy of allowing Plaintiffs the amount of all insurance checks cashed by the Willis Defendants is inconsistent with the equitable principles upon which a rescission-restitution claim must be based. Material injustice will be visited upon Defendants as a result.

II. Plaintiffs Have Not Refuted Defendants' Argument That the Court of Appeals Erred in Holding That Fraud in the Inducement Rendered The Insurance Power of Attorney Void *Ab Initio*.

In their application, Defendants have argued that the Court of Appeals erred in treating as void *ab initio* (i.e., as a nullity) the insurance power of attorney and related documents on the ground that Plaintiffs had been induced to sign the contract documents by fraudulent representations of the Willis Defendants that they were duly licensed. Defendants have cited established authority for the rule that fraudulent representations inducing the signing of a contract make a contract merely voidable, not void. In response, Plaintiffs have not attempted to explain where Defendants' legal reasoning is flawed and why the appellate decision was correct.

Plaintiffs have simply made the conclusory statement that the appellate ruling is in accordance with established precedents of this Court, citing the two cases that the Court of Appeals relied upon in its opinion, *Wedgewood v Jorgens*, 190 Mich 620, 622; 157 NW 360 (1916), and *Bilt-More Homes, Inc v French*, 373 Mich 693, 699; 130 NW2d 907 (1964).

The *Wedgewood* and *Bilt-More Homes* cases do not stand for the proposition (1) that fraud in the inducement in negotiating a contract renders the contract void *ab initio* or (2) that the unlicensed person's contract is a complete nullity from its inception. Instead, those cases merely hold that a person lacking a required professional license is barred from bringing a lawsuit to recover compensation for professional services. *Wedgewood* does recite that the agreement of a professional character without a required license is "illegal and void." Similarly, *Bilt-More Homes* says that contracts by an unlicensed residential builder are "not only voidable but void." However, the real holding in each case was that the unlicensed plaintiff could not pursue in court a claim for compensation for professional services. In Michigan, labeling the contract of an unlicensed professional as "void" or "illegal and void" only means that professional is unable to bring a lawsuit to collect monies due on his contract. In fact, all of the cases that Plaintiffs have cited for the proposition that the unlicensed builder's contract is not only voidable but void really only hold that the builder cannot pursue a court action. No case holds that the contract of the unlicensed builder is meaningless or ineffective between the homeowner and the builder.

The building contract is viewed as remaining in force since the homeowner can still sue for breach of contract to recover any damages caused by the builder's failure to comply with the contract. See, for example, *Roberson Builders, Inc v Larson*, unpublished Court of Appeals Docket No. 260039, 2006 WL 2683319 (2006), a copy of which appears in Plaintiffs' answer to the application. That the unlicensed builder's contract remains effective (and not a

nullity) is shown by the fact that, in *Roberson*, the homeowner pursued a lawsuit against the builder for breach of contract and recovered a verdict for \$24,048 based on substandard work and failure to complete certain work. The builder was permitted to defend the breach of contract lawsuit (although it was held that the builder could not pursue a claim for a setoff against the homeowner on an oral contract for certain extras requested by the homeowner.) In no reported Michigan case has a court ever treated the builder's contract as non-existent or invalidated any action taken by virtue of authority granted in the builder's contract papers.

The Court of Appeals opinion contained no citation of authority for its crucial conclusion that "Willis's fraud rendered the power of attorney entered by the Epps void *ab initio*." There is no legal support for that conclusion, which removed retroactively the authority of Willis to indorse the insurance checks. In their answer to the application, Plaintiffs were unable to cite any legal authority supporting the void *ab initio* conclusion. Defendants have found no case dealing with unlicensed builders or other unlicensed persons that strips their contractual rights with a ruling of voidness *ab initio*.

The Court of Appeals clearly erred in making the unsupportable legal ruling that the power of attorney in favor of Willis was void *ab initio*. That error has led to the further error that the Willis Defendants had no right under the power of attorney, or under the assignment language of the two work authorization documents, to indorse insurance checks relating to the work they were carrying out for Plaintiffs. These erroneous rulings led to the erroneous conclusion that Defendants committed conversion of the insurance checks and were liable to Plaintiffs for the face amount of each insurance check cashed with Denaglen.

It is appropriate for this Court to grant leave to appeal or summary reversal of the ruling

that Defendants are liable to Plaintiffs in conversion in the face amount of the insurance checks.

III. Plaintiffs Have Not Refuted the Argument That Damages for Conversion of An Instrument Are Limited to the Amount of Plaintiffs' Interest in the Instrument.

In their application, Defendants have correctly pointed out the error of the trial court and the Court of Appeals in ruling that the damages for conversion of the insurance checks were automatically the face amount of the checks allegedly converted by Defendants. Defendants cited the applicable subsection of MCL 440.3420 (which has governed causes of action for conversion of instruments under the Michigan UCC since September 30, 1993.) That subsection reads as follows:

(2) In an action under subsection (1) [for conversion of an instrument], the measure of liability is presumed to be the amount payable on the instrument, but **recovery may not exceed the amount of the plaintiff's interest in the instrument.** [Emphasis added.]

Commentators have pointed out that this provision has greatly changed the prior rule of automatically awarding conversion damages in the face amount of the converted instrument. Now, if the monies from a check end up going for the purpose that was intended, no damages may be awarded simply because an indorsement to a check was unauthorized or missing.

A leading treatise on the UCC explains that UCC 3-420(b) [MCL 440.3420(2)] has the beneficial effect of avoiding a windfall for a payee of a check when the proceeds of the check end up in the hands of the person for whom they were intended. White, Summers & Hillman state as follows regarding UCC 3-420(b):

We [e]ndorse judicial adoption of the proposition that there should normally be no recovery when the check proceeds come into the hands of the person for whom they are intended. A number of cases stand for the proposition that neither the drawer nor an intended payee of check paid over a forged or inadequate indorsement may maintain a conversion action **when the funds ultimately reach or benefit the intended payee.** [2 J. White, R. Summers & R. Hillman, Uniform Commercial Code: Practitioner Treatise Series (6th ed. 2013), § 19:9, p. 356. Emphasis added.]

In this case, all, or almost all, of the proceeds of the insurance checks was intended to go the Willis Defendants to fund their cleanup and construction work relating to Plaintiffs' home and the damaged contents. Plaintiffs benefited from having the monies go to the Willis Defendants to fund the work on the house. Accordingly, the damages recoverable for the alleged conversion of insurance proceeds checks would not be in the face amount of the checks that Defendant Willis cashed at Defendant Denaglen. Factual issues existed as to the amount of the benefit that Plaintiffs received from the monies that went to the Willis Defendants to fund the work and how much money the Willis Defendants were entitled to keep under their agreements with Plaintiffs. In view of the factual issue as to the amount of damages recoverable by Plaintiffs, it was improper for the trial court and the Court of Appeals to award judgment to Plaintiffs without a trial on the issue of damages. See *American State Bank v Union Planters Bank, NA*, 332 F3d 533, 538 (CA 8, 2003), applying UCC 3-420(b) and holding that summary judgment was inappropriate in a check conversion case where a factual issue existed as to the amount of benefit the plaintiff received from the converted check proceeds. The trial court and the Court of Appeals clearly erred in holding that Plaintiffs were entitled to recover judgment against Denaglen and the Willis Defendants for the face amount of the checks and that no trial was necessary on the issue of damages.

IV. Plaintiffs Are Incorrect in Their Statements About Purported Factual Inaccuracies in Defendants' Application or About Injecting New, Unpreserved Issues into This Appeal.

In their answer to the application, Plaintiffs charge that Defendants' counsel is fast and loose with his recitation of the facts involved in this case. That charge is false.

Also, Plaintiffs are mistaken in asserting that Defendants have not preserved the appellate issues raised in their application. For example, Defendants have not relied solely upon the

insurance power of attorney as authority for Defendant Willis to indorse the insurance checks. They raised below the fact that Plaintiffs in the work authorization document assigned to the Willis Defendants all of their rights in the insurance proceeds in full payment for the cleaning and restoration work. See ¶ 5 of affirmative defenses of the Willis Defendants filed Jan. 4, 2010. At page 5 of their brief in support of motion for partial summary disposition (filed May 13, 2011), the Willis Defendants pointed out that the work authorization executed “assigns the proceeds” of Plaintiffs’ insurance claim to Defendant 4 Quarters as “full payment” for the work authorized by the insurance company. That the assignment deprived Plaintiffs of any further interest in the insurance proceeds was raised in Plaintiffs’ appeal brief below at p. 5.

Likewise, Plaintiffs have previously cited MCL 440.3420(2) and argued that recovery for conversion of an instrument “may not exceed the amount of the plaintiff’s interest in the instrument.” In its summary disposition brief filed below (p. 7), Defendant Denaglen cited MCL 440.3420(2) and argued that Plaintiffs had no more interest in the insurance check proceeds and no right to damages since the funds were applied toward payment of the amounts due to the Willis Defendants for the repair work. In their appellate brief below, Defendants continued to assert that Plaintiffs did not have any cognizable damages for conversion because Plaintiffs had no more interest in the insurance checks after the funds were applied to the obligations owing to the Willis Defendants for the restoration work.

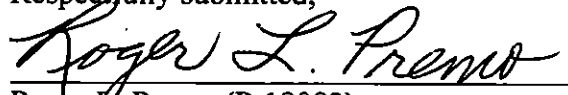
Plaintiffs also incorrectly assert that Defendants never previously raised the issue that the contract documents of the Willis Defendants were not void and ineffective because of their lack of a license. Defendants have consistently argued that the power of attorney and the assignment of the check proceeds were effective to allow Willis to indorse the insurance checks and to apply the funds to the amounts owed to the Willis Defendants for the restoration work. See pages 1

and 2 of Defendants' appeal brief in the Court of Appeals pointing out that the Willis Defendants were entitled to receive the insurance proceeds by virtue of the insurance power of attorney and the assignment of insurance proceeds in the work authorization document. Defendants have never conceded that the insurance power of attorney and the assignment documents were invalid simply because Plaintiffs' counsel contended that the contract documents were "void" because of the unlicensed status of the Willis Defendants. Defendants have always taken the position that cases stating that the contract of the unlicensed builder is "void" merely mean that the unlicensed builder is barred from bringing a lawsuit to collect compensation and nothing more. Moreover, the issue of whether fraud in the inducement renders contract documents void *ab initio*, and not merely voidable, was injected into the case by the Court of Appeals opinion affirming the judgments below on an alternate ground. Since Defendants disagree with the analysis of the Court of Appeals as to the fraud in the inducement theory, it was perfectly appropriate for Defendants to raise their disagreement with the new analysis of the Court of Appeals in the application for leave to appeal.

RELIEF REQUESTED

Defendants-Appellants Denaglen Corp., Troy Willis, 4 Quarters Restoration, LLC, and Emergency Insurance Services request that this Court grant leave to appeal on all of the issues addressed by Defendants-Appellants in this Application or in the alternative grant peremptory relief in favor of Defendants-Appellants on those issues.

Respectfully submitted,



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Date: November 15, 2013

PROOF OF SERVICE

ROGER L. PREMO hereby certifies that on November 15, 2013 he served a copy of Defendants-Appellants' Reply Brief In Support Of Application For Leave To Appeal and this Proof of Service upon Gerald F. Posner, Esq., attorney for Plaintiffs-Appellees, by first-class mail directed to his office address at 1400 Penobscot Building, Detroit, MI 48226.


Roger L. Premo

Date: November 15, 2013